CIA/OER/S-06834-75 FACTORS BEARING ON PORTUGAL'S VULNERABILITY

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FACTORS BEARING ON PORTUGAL'S VULNERABILITY TO ECONOMIC SANCTIONS

The following information is provided in response to your question concerning the vulnerability of Portugal to economic sanctions:

- In 1973 exports were $1.9 billion or one-sixth of GNP.
- Imports (fob) were $2.6 billion or one-fourth of GNP.
- The trade balance, tourism, and worker remittances all turned for the worse in 1974.
- Foreign exchange reserves fell from $2.8 billion at the end of 1973 to $2.3 billion at the end of November.
- Principal imports include petroleum, cotton, industrial machinery, iron and steel, and chemicals.
- Principal exports include cotton textiles, cork and cork products, canned fish, wine, timber, paper, and wood products, and resin.

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PORTUGAL: PRINCIPAL TRADING PARTNERS IN 1974*

IMPORTS

Overseas territories and former territories	10.4%
European Community	44.4%
Of Which:	
West Germany	13.6%
United Kingdom	9.6%
France	7.8%
Italy	5.5%
EFTA	9.3%
Spain	4.3%
European Communist Countries	1.4%
USA	9.2%
Canada	0.7%
Latin America	4.8%
Iran	3.9%
Iraq	3.2%
Japan	3.0%

EXPORTS

Overseas territories and former territories	10.9%
European Community	48.8%
Of Which:	
West Germany	7.7%
United Kingdom	23.0%
France	5.8%
Italy	3.5%
EFTA	14.7%
Spain	2.0%
European Communist Countries	0.9%
USA	10.5%
Canada	1.3%
Latin America	3.1%
Japan	1.5%
Other Asia	2.1%

*January-November

PORTUGAL: ECONOMIC PROBLEMS, UNCERTAIN SOLUTIONS

Political turmoil has been the single most important factor affecting Portuguese economic developments since a military-led coup ended 50 years of authoritarian rule last April. Efforts to grapple with economic problems will be ineffectual until the political direction in Lisbon steadies.

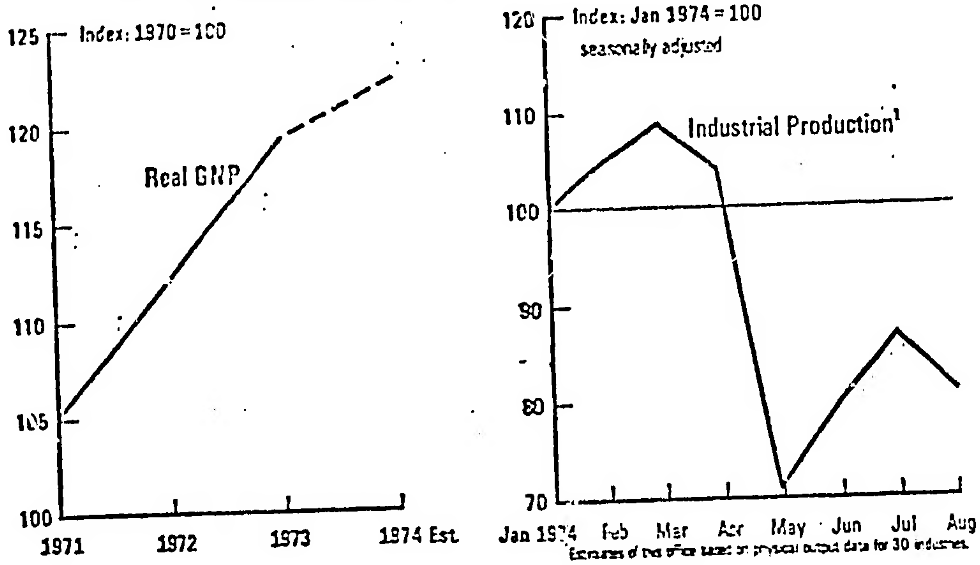
Recent Developments

Production data are sparse, a reflection of the new government's inability to cope with administrative detail amid continuing political upheaval. As best we can determine, industrial production has begun to recover from the estimated 35% plunge in the six weeks following the coup. Strikes have subsided since late summer, partly because workers have been pacified by huge wage increases. At the same time, tourism and other important activities remain depressed.

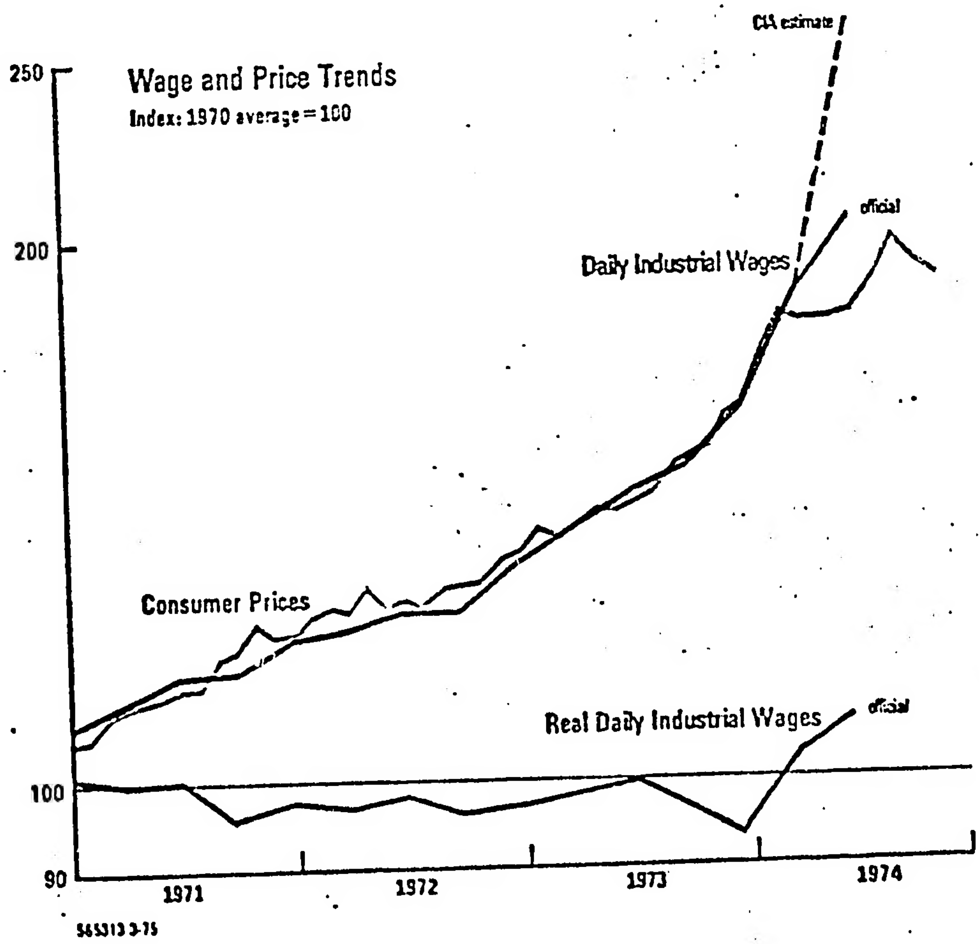
Unemployment is now the most critical economic problem. The growing body of jobless workers, mostly unskilled and uneducated, constitutes a particularly volatile element in the political tinderbox. At yearend, perhaps 200,000 people – 7% of the labor force – were idle. The sharp increase in unemployment is the result of a combination of factors: industrial slowdown and political turmoil at home, worldwide recession, return of soldiers and settlers from the African provinces, and the diminishing ability of North European countries to absorb surplus Portuguese laborers.

PORTUGAL

GNP and Industrial Production



[1] Estimates of this office based on physical output data for 30 industries.



Portugal: Balance of Payments

Million US $

	1971	1972	1973	1974[1]
Exports	955	1,353	1,927	2,160
Imports (f.o.b.)	1,584	1,947	2,642	3,460
Trade balance	-629	-594	-721	-1,300
Tourism	212	261	320	250
Other services	-73	-56	-157	-230
Transfers	664	873	1,097	1,000
Current account balance	174	484	539	-280
Long-term capital, private	76	62	-37	
Long-term capital, public	-12	-191	-104	-300
Short-term capital	-6	-137	0	
Errors and omissions	35	60	-56	
Surplus or deficit	267	278	342	-580

1. Estimated.

Inflation continues to be worse than in most Western countries; consumer prices went up about 25% last year despite a temporary price freeze following the coup. Wages lagged behind the price spiral until April. The drop in real wages was especially pronounced in the half year preceding the coup. This situation has changed sharply. The official wage index for the third quarter showed a 39% gain over the year-earlier level – more than offsetting the rise in prices. We estimate an even greater increase in wages in the quarter – an average of 75% in the 12 largest industries.

The trade deficit nearly doubled in 1974, to an estimated $1.3 billion. The rise in oil costs accounted for half of this increase. Net food imports jumped by $230 million because of higher consumption by low-income groups. A one-third increase in the traditional net earnings from paper, textile, and wood products, to $450 million, offset only a small part of the rise in imports. With invisible earnings also declining, the current account shifted from a $540 million surplus to a deficit of about $280 million. In addition, capital flight helped to push the deficit in the capital account to an estimated $300 million.

Outlook

The power struggle between moderates and leftists may be settled through elections for a constitutional assembly, now scheduled for 12 April, and through

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the legislative elections in the fall. In the interim, the Gomes government is trying – not very successfully – to boost business confidence by pursuing a middle course. It has promised that a large part of the economy will be left to private enterprise, including foreign investors. A sharp increase in the government's economic role nonetheless is in the cards. At the minimum, Lisbon probably will assume control of natural resources, telecommunications facilities, and the energy industries.

Private enterprise can be expected to prolong its wait-and-see attitude until the political situation stabilizes. Mobil, Exxon, and Dow Chemical are among the firms that have canceled or deferred investment projects.

The jobless rate is likely to reach 10% this year as more soldiers return and a new crop of young people enter the labor force. To prevent still higher unemployment, Lisbon is pressing EC countries to be as accommodating as possible on the issue of immigrant workers.

The spiral of higher money wage rates and rapid price rises could be speeded up this year, especially in view of the government's weak political hold.

The trade deficit is expected to grow, while earnings from tourism and worker remittances continue to decline. Lisbon probably will obtain financial assistance from the EC and can also fall back on foreign reserves of $2 billion. It may also devalue the escudo, perhaps as part of an economic reform program of the government chosen next fall. 25X1